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SUBJECT: PAROCHIALISM AND THE STATE SECTOR LIMIT HUE'S ECONOMIC PROSPECTS

REF: A) HCMC 623; B) HCMC 586; C) 04 HCMC 1528; D) 04 HCMC 1270

1. (SBU) Summary: Party and local government leaders of the central Vietnam province of Thua Thien Hue extolled the economic potential of the province to Consul General May 23-24. The potential is clearly there -- Hue has the attributes to become a tourism and knowledge-based economy leader. However, unless Hue's leaders show greater initiative, particularly in breaking the province from its dependency on inefficient state-owned enterprises, the province will continue to be eclipsed by its more aggressive and pro-business neighbors to the south. End Summary.

2. (SBU) On May 23-24, the Consul General made official calls on the provincial leadership of the central province of Thua Thien Hue, the northernmost province in HCMC's consular district. He met with the Vice-Chairman of the People's Committee Nguyen Ngoc Thien, Provincial Party Secretary Ho Xuan Man, and Deputy Director of the provincial Department for Planning and Investment (DPI) Le Dinh Khanh. The CG also met with the Director of the University of Hue Nguyen Vien Tho, past participants in the International Visitor's program, and the seven Americans resident in Hue. Economic development and religious freedom were core focuses of the visit. (Religious freedom issues in Hue are covered in refs A and B.)

Local leadership: Proud and Comfortable

3. (SBU) In their official presentations, Thua Thien Hue's party and provincial government leaders emphasized that the province has the attributes to become Vietnam's premier tourism and services-sector magnet: a low-cost, well educated workforce; a comprehensive university system; beaches, mountains and national parks; and some of Vietnam's most impressive cultural and historical heritage sites. They acknowledged that infrastructure needs further upgrading, but is sufficient to support development. They were convinced that the June 2005 opening of the 4.6 kilometer Hai Van tunnel will spur growth as Hue becomes better integrated into the regional economy, particularly with the harbor and international airport in neighboring Danang.

4. (SBU) Provincial leaders said that their economic stewardship has been effective; Per capita GDP had reached USD600 and GDP growth was over nine percent in 2004. In 2004 the industrial sector grew by 16 percent, agriculture by four percent and services, including tourism, by 6 percent. Hue attracted over one million domestic and international tourists in 2004. They added that in the first five months of 2005, tourist arrivals were up 30 percent from the comparable period in 2004.

5. (SBU) Hue's leaders were in the throes of shaping the province's 2006-2010 five-year plan. They had not yet decided what the major emphasis should be: industry and the related infrastructure it requires -- such as an expanded deep-water port -- or tourism. The provincial Party Chairman explained that the ultimate shape of the plan would depend on how the Party applied Hanoi-level guidance to local conditions and assessed the various "potentials" that each sector has to offer. Our follow-on briefing at the DPI reflected the uncertainty about Hue's economic direction. The DPI Director told us that the province was seeking investments in sectors as varied as: informatics, biotech, resorts, eco-tourism, industrial parks, aquaculture, health care and handicrafts manufacture. All were priorities.

Numerous requests for U.S. assistance

6. (SBU) Thua Thien Hue officials presented the CG with a laundry list of assistance requests: to help promote Hue with U.S. investors, secure ODA for infrastructure development, assist the province to build new health clinics, clear unexploded ordinance (UXO) remaining from the war, intercede with the State of Hawaii to speed up ratification of a pending cooperation agreement, and help the Hue University system develop collaborative relationships with U.S. academic institutions.

7. (SBU) In his official meetings and press outreach, the CG welcomed and encouraged Hue's efforts to expand ties with the United States. Our bilateral economic relationship is growing rapidly and there is no reason why Hue cannot participate much more fully in this success story. That said, it was up to Hue to promote Hue. More broadly, the province should not make a distinction between domestic and foreign investors; rather, it

should create a climate conducive for business. Foreign investors go where domestic entrepreneurs succeed, the CG emphasized. Similarly, Hue's educational institutions needed to do a better job of leveraging their contacts with U.S. institutions to develop long-term partnerships. The CG observed that Hue should look to the market, not ODA, to satisfy its infrastructure needs. While concessional ODA may seem attractive at first blush, ultimately the projects may not be as cost effective. Finally, the USG supported Vietnam's efforts to deal with war-legacy issues such as UXO removal. If there was a need for U.S. assistance, the Hue provincial government needed to make its case to the GVN first.

SOE Domination -----

18. (SBU) Thua Thien's Hue's economy is dominated by state-owned enterprises (SOEs). Even in the tourist sector, almost all the province's major hotels are either fully state-owned or the local government has a controlling interest. Although the People's Committee Vice Chairman emphasized that the province is committed to expanding the private sector, since 2000 when the Enterprise Law was passed, the province has registered 1000 private enterprises, 348 in 2004. Of these, only 10 percent have assets of more than USD 70,000. (In 2004, over 37,000 private enterprises were registered nationwide; HCMC receives 10 to 15 new registration applications every day.) To date, the province has attracted only 30 FDI projects with a total registered capital of USD 170 million. Five U.S. FDI projects have been licensed, but only one is operating. Despite Hue's reputation as a university town, only one small software developer has set up shop in the province with a capital investment of USD 20,000, the DPI reported.

Industry: Lagging Behind -----

19. (SBU) If Thua Thien Hue's industrial sector grew by 16 percent in 2004, it did so from a very small base. A tour of Phu Bai industrial park, which according to its Director is one of the province's development centerpieces, made it clear that tourism, not industry, is Hue's competitive advantage. Established in late 1998, the industrial park had a few operational factories, a handful more under construction and many more empty lots. The park had none of the bustle that we saw in the export processing zone in neighboring Danang, let alone the scope of industrial activity in HCMC and its neighboring provinces (refs C and D). A project that was touted to us as being "Chinese FDI," was in reality, a 70 percent Vietnamese investment, with a minority Chinese stakeholder. That investor, a businessman from HCMC, told us that he invested in Hue out of a sense of obligation to his family's native province. He convinced his long-time Chinese partner to take a 30 percent stake in the factory, which makes inexpensive ceramic ware for the domestic market. While he is not losing money, his factories in the HCMC area were more productive and profitable he said, despite a 50 percent wage premium. Other domestic investors have no reason to come to Hue, he said privately.

Tourism: Growing But Lackluster -----

110. (SBU) Despite all it has to offer, at the moment Hue is an also-ran to the smaller and less culturally and historically endowed coastal town of Hoi An, located some 60 miles to the south in Quang Nam province. Tourists vacation in Hoi An. They visit Hue for the day or stay overnight. Hoi An has a lively yet dignified "scene" and a variety of shops to extract maximum revenue from tourists. Tourists and developers -- domestic and foreign -- have invested in the Hoi An/Danang corridor because Hoi An has marketed itself extremely well and the Quang Nam and Danang provincial governments have established pro-business reputations. In contrast, despite the importance of the tourism sector to the local economy, Thua Thien Hue province has just approved the first FDI hotel project, a Dutch resort outside Hue city.

Comment -----

111. (SBU) Hue's leaders are right when they claim that the province has all the physical attributes to become a tourist Mecca. They are rightly proud of and determined to preserve Hue's reputation as a socially conservative, cultural and historical center of Vietnam. What Hue lacks are the intangibles needed to put it on a path of high economic growth. Its leaders lack vision and self-confidence. They are rooted heavily in the "Party planners know best" philosophy of management. Their repeated requests for assistance demonstrated a naivete about how the world outside Hue works. The Provincial Competitiveness Index on the Business Environment in Vietnam, a product of the USAID-funded Vietnam Competitiveness Initiative (VNCI) reflects the province's lackluster approach to business: the province was ranked well below neighboring Danang and industrial dynamos Dong Nai and Binh Duong.

112. (SBU) Despite successful models elsewhere in southern Vietnam, state control and caution are still seen as the route to

job security by many provincial leaders in Vietnam. Hue's leaders are no exception. They feel no pressure to change their way of doing business. The province's state-run hotels are making some money and the economy is on an upswing. The Party and the SOE managers enjoy their sinecures safe from the pressures of competition with the private sector. Hue provides another example that profitable but inefficient SOEs are more of threat to the economy than their bankrupt brethren. Hue cannot afford to be complacent. If the province does not work hard to capitalize on its cachet and make the province more appealing for long-term vacationers, the newly opened Hai Van tunnel might actually erode the Hue tourist market as day trips from Danang and Hoi An become that much more convenient.

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